Rob Frost

Lessons from Brexit – Implications for Governance and Risk

The UK vote to leave the European Union has created uncertainty and potential volatility around the world. As the implications of the vote continue to unfold, businesses are being urged to consider the near and long-term effects on the risk environment, strategic direction, and potential workforce dislocation.

But it is not only this vote that should prompt boards and management to reconsider the issues that are going to impact their businesses and future success. In many respects, this vote reflects a mix of more fundamental trends that are emerging globally and already impacting the regions and markets in which our companies operate.

Jean-Pierre Lehmann, founder of the Evian Group, recently said in an article in the South China Morning Post, "Brexit is a window into a future where ageing populations hang on to their privileges and global economic growth has failed to benefit all". He noted that:

- The disintegration of the EU is now practically irreversible

- Brexit illustrates the power of gerontocrats, evident in East Asia as well as Europe. For China, a market particularly key to New Zealand, the effects of the one-child policy are significant and are now being more clearly understood.
- The result reflects the rising tide of deglobalisation.

Populism is evident in many countries and is driven by both economic and social factors. The US Presidential election race is also clearly demonstrating how some of these global issues are gaining significant traction across large parts of an electorate that traditionally have not been prominent or vocal.

Since the end of World War II, international trade has been the engine that has driven growth and economic prosperity, not always consistently, across both the developed world and portions of the third world. However, the economic discontent that some Trump supporters reflect (and was clearly evident in the Brexit vote) highlights that the economic benefits flowing from globalisation are not being shared evenly and fairly across both countries and workforces. As a result, we see Donald Trump's threat to pull the US out of the WTO. Even Hillary Clinton recognises that this issue is sufficiently major that she must now consider taking a stance.

What are the odds on TPP progressing now? Other potential New Zealand agreements seeking better access to markets, might also become less likely.

These underlying global issues can have a significant impact on corporate New Zealand and should be on company strategic risk radars and taken into account during strategic planning. The timing and ultimate nature of such events, which could turn out to have both positive and negative implications for corporate New Zealand, are very hard to estimate.

However, does this uncertainty mean that it is not worth committing resources to better understand and assess the potential opportunities and threats they represent? In the UK and US these trends have already given rise to significant change that will likely impact company performance, both positively and negatively.

Formal risk management disciplines can help; they are the capabilities that are best suited to support smarter navigation of the uncertain waters ahead. They provide a structured manner in which uncertainty (and we have plenty of that) can be considered in the context of a company's strategic objectives. Risk advisors, and wise heads that can support more complex planning and decision analysis needs, will be in high demand.

The ability to build resilience into an organisation, or position a business to seize potential opportunities, is becoming increasingly difficult due to the volatility and velocity of issues that impact performance. It's now evident that many of the key political and social events that make up the headlines reflect deep-seated issues that will be around for some time and need to be considered in our planning. There is vocal support for any politician who promises these issues will be addressed.

WHAT SHOULD COMPANIES BE DOING NOW?

The consequence of the UK exit from the EU could be significant and should be assessed. Companies with strategic objectives that are dependent on trade with Europe, access to Europe via the UK and freedom of people movement are at greater risk. Shareholders are likely to be already nervous. Planning appropriate mitigation is imperative. But where Brexit is concerned, there may be ample time with exit negotiations forecast to take many years.

Could the Brexit vote, the rise of populism supporting right-wing politicians and the rising tide of de-globalisation signal the likelihood of further EU fragmentation? How will New Zealand companies respond to an environment where new free trade agreements are no longer possible? Or existing agreements are under threat?

Good risk management is about anticipating issues and being proactive. We are in an environment where investing in strengthening risk capabilities is not just prudent to do, it will be critical to do. New Zealand businesses should be poised to move faster and better than competitors if they want to seize the opportunities that arise out of the uncertainty. It will also be important to ensure any negative consequences are identified well in advance and appropriately planned for. Competitive advantage is the reward.

The responsibility for being proactive does not only rest with executive management. Directors carry clear responsibility for risk oversight, strategic effectiveness and performance. They need to be ensuring that formal structured thinking is underway within the company to understand the implications of the issues that we are seeing globally.

Risk management though is not about planning; it is about taking better decisions now that strengthen an organisation for tomorrow. It is a structured process to identify, assess, treat and monitor risk. Just having a list of a dozen or so risks now will not add much value. The global issues highlighted here will have an impact in the medium or longer term planning horizons for most companies. However, the nature of the risk and a company's exposure to it will change over time as more is learned about a risk and its potential impact on a business. Initiatives considered now will likely have to be modified over time as additional clarity is gained; risk management is a continuous process.

With the uncertainty we face and the spectrum of significant global trends in play, risk management disciplines are an increasingly important input to the major decisions that companies will be making.

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